

## Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 ISO-00 SP-02 AID-05 EB-07 NSC-05  
EPG-02 SS-15 STR-04 OMB-01 CEA-01 CIAE-00 COME-00  
FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 LAB-04  
SIL-01 L-03 H-01 PA-01 PRS-01 USIE-00 SSO-00  
INRE-00 NSCE-00 EURE-00 DODE-00 PM-05 IO-13 /106 W  
-----002419 201932Z /40

O R 201717Z JUL 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 6001

TREAS DEPT WASH DC IMMEDIATE

INFO AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMCONSUL MILAN

AMCONSUL NAPLES

AMEMBASSY PARIS

AMEMBASSY THE HAGUE

AMEMBASSY TOKYO

USDOCOSOUTH

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AMCONSUL GENOA

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AMCONSUL TURIN

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STATE PASS FRB; BRUSSELS ALSO FOR EC; PARIS ALSO FOR OECD;  
USDOCOSOUTH FOR INTAF

E.O. 11652: N/A

TAGS: EFIN, IT

SUBJECT: ITALIAN PERFORMANCE UNDER IMF AND EC LOANS

1. SUMMARY. THIS IS THE FIRST IN A SERIES OF PERIODIC

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REPORTS ON ITALIAN PERFORMANCE UNDER THE IMF STANDBY  
AGREEMENT OF SDR 450 MILLION AND UNDER OUTSTANDING EC LOANS  
TO ITALY (THE MOST RECENT OF WHICH WAS A \$500 MILLION JOINT  
BORROWING). AN AIRGRAM FOLLOWS GIVING HISTORIC DATA FOR  
EACH TARGET AND AN EXPLANATION OF THE METHODS USED BY THE  
EMBASSY IN ASSESSING ITALY'S PERFORMANCE. THE FOLLOWING  
ARE THE CHIEF CONCLUSIONS OF THIS REPORT BASED ON THE

LASTEST DATA AVAILABLE (MAINLY FOR THE FIRST QUARTER OF 1977): (1) ITALY EXCEEDED ITS FIRST QUARTER EC TARGET FOR DOMESTIC CREDIT EXPANSION BY A SUBSTANTIAL AMOUNT AND MAY WELL ALSO EXCEED THE SECOND QUARTER TARGET. (2) DURING THE FIRST FOUR MONTHS OF THE YEAR, ITALY APPEARED TO BE WELL WITHIN THE CEILING ON THE TREASURY CASH DEFICIT. (3) DURING THE SAME PERIOD THE TREASURY ACTUALLY MADE REPAYMENTS TO THE CENTRAL BANK, RATHER THAN HAVING TO BORROW. (4) FIVE-MONTH DATA SUGGESTS THAT ITALY'S PERFORMANCE IS CONSISTANT WITH ITS ANNUAL CEILING ON CENTRAL GOVERNMENT CASH EXPENDITURES. (5) ITALY ALREADY HAS A MARGIN OF 1 POINT AND WILL LIKELY HAVE AN ADDITIONAL 1-POINT MARGIN AGAINST ITS FIRST AND SECOND QUARTERLY CEILINGS ON THE INCREASE IN THE COST-OF-LIVING WAGE ESCALATOR INDEX. (6) DURING THE FIRST QUARTER ITALY'S DEFICIT ON CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS SEEMED TO BE CONSISTENT WITH ACHIEVEMENT OF ITS IMF TARGET OF A SURPLUS OF 500 BILLION LIRE DURING THE STANDBY YEAR. IN SUM, EXCEPT FOR DOMESTIC CREDIT EXPANSION, ITALY SEEMS ON TARGET VIS-A-VIS ITS INTERNATIONAL COMMITMENTS. END SUMMARY.

2. DOMESTIC CREDIT EXPANSION. SINCE THE IMF'S COMMITMENT FOR THIS ITEM COVERS THE STANDBY YEAR BEGINNING APRIL 1, 1977, THERE WAS NO IMF TARGET FOR THE FIRST QUARTER OF CY 1977. HOWEVER, THERE WAS A FIRST QUARTER EC TARGET, LIMITED OFFICIAL USE

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WHICH WAS EXCEEDED BY 1,247 BILLION LIRE. FIR THE FIRST HALF OF EC TARGET YEAR (JANUARY-JUNE 1977), DATA FOR APRIL ALSO SUGGEST THAT ITALY MAY EXCEED THAT TARGET SINCE A MARGIN OF ONLY 1,788 BILLION LIRE PER MONTH REMAINS FOR MAY AND JUNE, AGAINST AN AVERAGE MONTHLY FIGURE OF 2,681 BILLION LIRE THROUGH THE FIRST FOUR MONTHS OF THE YEAR. MARGIN FOR FORST IMF QUARTER IS 2,411 BILLION LIRE PER MONTH.

TABLE 1  
DOMESTIC CREDIT EXPANSION  
(BILLIONS OF LIRE)

| 1977       |       |                |        |
|------------|-------|----------------|--------|
| I          | II    | CY             |        |
| EC TARGET  | 6,100 | 8,200          | 30,600 |
| CUMULATIVE |       | 14,300         |        |
| IMF TARGET | -     | 8,200          | -      |
| CUMULATIVE |       |                |        |
| ACTUAL     | 7,347 | 3,377 (1 MO)   |        |
| CUMULATIVE |       | 10,724 (4 MOS) |        |

ITALY'S FAILURE TO COMPLY WITH THE FIRST QUARTER EC TARGET HAS BEEN THE SUBJECT OF ITALIAN PRESS DEBATE BASED UPON A LEAK OF AN EC COMMISSION DOCUMENT ABOUT TWO

WEEKS AGO. TREASURY MINISTRY SOURCES HAVE TOLD EMBASSIES  
THAT AN IMPORTANT REASON FOR ITALY'S HAVING EXCEEDED  
THE TARGET WAS THE LARGE INFLOW OF SHORT-TERM BANK  
CAPITAL WHICH WAS RE-LENT TO ITALIAN BORROWERS. HOWEVER,  
THEY ARGUE THAT THE PROCEEDS OF THESE LOANS WERE, IN  
TURN, USED TO REPAY LARGE AMOUNTS OF FOREIGN COMMERCIAL  
CREDITS DURING THE FIRST QUARTER. THUS, THE EXCESS OF  
CREDIT EXPANSION WAS NOT INFLATIONARY. THEY FURTHER  
CLAIM THAT THERE WILL BE A SLOWDOWN IN SUCH FOREIGN  
CAPITAL INFLOWS DURING COMING MONTHS AND THAT ITALY WILL  
BE ABLE TO GET BACK WITHIN ITS CEILINGS. (THESE WERE  
ARGUMENTS USED BY TREASURY MINISTER STAMMATI WITH OTHER  
EC MINISTERS OF FINANCE AT THEIR MEETING ON JULY 18.)  
WHILE TREASURY MINISTRY ARGUMENTS HAVE SOME VALIDITY,  
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AND THE CURRENT SLOWDOWN IN ECONOMIC ACTIVITY MAY REDUCE  
DEMAND FOR CREDIT LATER THIS YEAR, THE EMBASSY IS RATHER  
DOUBTFUL ABOUT ITALY'S LIKELY COMPLIANCE WITH THESE CEILINGS.

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O R 201717Z JUL 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 6002

TREAS DEPT WASH DC IMMEDIATE

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STATE PASS FRB; BRUSSELS ALSO FOR EC; PARIS ALSO FOR OECD;  
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3. PUBLIC SECTOR CASH DEFICIT. ALTHOUGH THERE IS AN  
 IMF/EC CEILING FOR THE "ENLARGED" CASH DEFICIT OF 16,450  
 BILLION LIRE FOR 1977, THERE ARE NO QUARTERLY SUB-CEILINGS  
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AND NO PUBLISHED DATA ON THIS MEASUREMENT OF THE DEFICIT.  
 CONSEQUENTLY, THESE EMBASSY REPORTS WILL ONLY COVER THE  
 "NET TREASURY DEFICIT". ALTHOUGH THERE IS NO EXPLICIT GOI  
 FORECAST FOR THIS DEFICIT IN THE FIRST QUARTER, IT APPEARS  
 FROM ACTUAL DATA THAT THE SIZE OF THE DEFICIT WAS WELL IN  
 LINE WITH THE PROJECTED DEFICIT FOR THE FIRST HALF. THIS  
 CONCLUSION IS SUPPORTED BY A PRELIMINARY FIGURE FOR  
 APRIL WHICH SHOWED A CUMULATIVE FOUR-MONTH DEFICIT OF  
 4,738 BILLION LIRE AGAINST A FIRST HALF TARGET OF 8,700  
 BILLION LIRE. THE ACTUAL DATA ALSO SEEM TO BE IN LINE  
 WITH THE IMF SUB-CEILINGS ON "OTHER TREASURY OPEATIONS"  
 AND ON THE PART OF ORDINARY TREASURY OPERATIONS WHICH CON-  
 SISTS OF FINANCING OF THE DEFICITS OF MUNICIPAL GOVERN-  
 MENTS. ALTHOUGH PERFORMANCE SO FAR APPEARS TO BE GOOD,  
 IT SHOULD BE BORNE IN MIND THAT THE QUARTERLY CEILINGS  
 DROP RATHER SHARPLY FOR THE LAST TWO QUARTERS OF 1977.

TABLE 2  
 PUBLIC SECTOR CASH DEFICIT  
 (BILLIONS OF LIRE)

| 1977                     |        |               |         |  |
|--------------------------|--------|---------------|---------|--|
| ACTUAL                   |        | IMF/EC TARGET |         |  |
| I                        | II     | CY            |         |  |
| BUDGET DEFICIT           | -3,674 | N/A           | -9,900  |  |
| OTHER TREASURY OPS.      | 805    | N/A           | -3,500  |  |
| TOTAL TREASURY DEFICIT   | -2,869 | -1,912(1 MO)  | -13,400 |  |
| NET TREASURY DEFICIT(1)  | -2,826 | N/A           | -13,100 |  |
| HEALTH, HOSPITAL, SOCIAL | N/A    | N/A           | -3,350  |  |
| SECURITY AND ENEL        |        |               |         |  |
| ENLARGED DEFICIT         | N/A    | N/A           | -16,450 |  |

1) EXCULEDS TREASURY LEADING TO SPECIAL CREDIT INSTITUTES.

N/A - NOT AVAILABLE.

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4. CNETRAL BANK FINANCING OF TREASURY DEFICIT. DATE THROUGH THE FORST FOUR MONTHS OF THE YEAR SHOW SUBSTANTIAL REPAYMENTS TO THE CENTRAL BANK BY THE TREASRUY (591 BILLION LIRE) COMPARED TO AN ANNUAL CEILING OF 4,000 BILLION LIRE IN CREDITS FROM THE CENTRAL BANK TO THE TREASRUY. THIS GOOD PERFORMANCE IS OWED TO THE FACT THAT THE TREASURY HAS BEEN ABLE TO FINANCE A LARGE PART OF ITS DEFICIT THROUGH SALES OF TREASURY BILLS TO THE BANKS AND THE PUBLIC, PERMITTING THE BANK OF ITALY TO REDEEM MATURING TREASURY BILLS (I.E., REDUCE ITS NET CREDIT TO THE TREASTURY). SO LAONG AS THE MARKET FOR TREASURY BILLS REMAINS FAVORABLE, AS IT MAY FOR THE REST OF THE YEAR, THE PROSPECTS ARE FAIRLY GOOD THAT ITALY WILL BE ABLE TO MEET THIS EC TARGET. (NOTE, HOWEVER, THAT THE EC CEILING OF 4,000 BILLION LIRE IS VERY LOW COMPARED TO ACTUAL CENTRAL BANK FINANCING OF THE TREASURY IN RECENT YEARS, WHICH AVERAGED 8,419 BILLION LIRE IN THE PERIOD 1974-1976.)

TABLE 3  
CENTRAL BANK FINANCING OF TREASURY DEFICIT  
(BILLIONS OF LIRE)

| 1977       |      |              |       |
|------------|------|--------------|-------|
| I          | II   | CY           |       |
| EC TARGET  | -    | -            | 4,000 |
| CUMULATIVE | -    | (2,650)(1)   |       |
| ACTUAL     | -515 | -76 (1 MO)   |       |
| CUMULATIVE | -    | -591 (4 MOS) |       |

1) EMBASSY ESTIMATE OF SIX MONTH IMPLICIT TARGET BASED ON RATION OF CENTRAL BANK FINANCING CEILING TO TREASURY DEFICIT TARGETS.

5. CENTRAL GOVERNMENT CASH EXPENDITURES. THROUGH THE FIRST FIVE MONTHS OF THE YEAR, ITALY APPEARED TO BE WELL LIMITED OFFICIAL USE

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WITHIN THE EMBASSY'S ESTIMATED PATTERN OF 1977 CENTRAL GOVERNMENT CASH EXPENDITURES WHICH WOULD BE NECESSARY FOR ITALY TO CONFORM TO THE IMF/EC CEILING OF 55,350 BILLION LIRE.

NOTE, HOWEVER, THAT THERE ARE NO QUARTERLY TARGETS NOR DOES THE EMBASSY HAVE ANY OFFICIAL FORECASTS OF QUARTERLY DATA. CONSEQUENTLY, IT HAS HAD TO MAKE ITS OWN ESTIMATES OF IMPLICIT TARGETS WHICH WOULD APPEAR TO CONFORM TO THE ANNUAL CEILING. BASED ON THESE IMPLICIT TARGETS, ITALY HAD A MARGIN OF 4,475 BILLION LIRE REMAINING FOR THE FIRST HALF (I.E. JUNE) COMPARED TO THE MONTHLY AVERAGE OF 4,375 BILLION LIRE RECORDED DURING THE FIRST FIVE MONTHS OF 1977.

TABLE 4  
CENTRAL GOVERNMENT CASH EXPENDITURES  
(BILLIONS OF LIRE)

| 1977                   |        |                |        |
|------------------------|--------|----------------|--------|
| I                      | II     | CY             |        |
| IMF TARGET             | N/A    | N/A            | 55,350 |
| EMBASSY QTLY. ESTIMATE |        | 14,340         | 12,010 |
| CUMULATIVE             |        | 26,350         | 55,350 |
| ACTUAL                 | 15,226 | 6,649 (2 MOS)  |        |
| CUMULATIVE             |        | 21,875 (5 MOS) |        |

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O R 201717Z JUL 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 6003

TREAS DEPT WASHDC IMMEDIATE

INFO AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMCONSUL MILAN

AMCONSUL NAPLES

AMEMBASSY THE HAGUE

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AMCONSUL GENOA

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6. COST-OF-LIVING ESCALATOR INDEX. THE ONLY IMF TARGET IN THE AREA OF WAGES AND PRICES CONSISTS OF CEILINGS ON INCREASES IN THE COST-OF-LIVING ESCALATOR INDEX (SCALA MOBILE). IMF QUARTERLY TARGETS (WHICH ARE MEASURED FROM MID-MONTH TO MID-MONTH) ASSUME CERTAIN NUMBER OF POINT INCREASES PER QUARTER. ACTUAL DATA FOR THE FIRST OF THESE QUARTERS SHOWS THAT ITALY REMAINED BELOW CEILING BY 1 POINT. PRESS REPORTS INDICATE THAT THE PROBABLY

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INDEX FOR THE SECOND QUARTER WILL ALSO BE 1 POINT BELOW THE IMF CEILING. THUS, IT WOULD APPEAR THAT ITALY WOULD HAVE A 2-POINT MARGIN BUILT UP DURING THE FIRST TWO IMF QUARTERS. FOR THE ENTIRE CALENDAR AND STANDBY YEARS, THE LATEST PRICE MOVEMENT DATA SEEM SOMEWHAT BETTER THAN ORIGINALLY ANTICIPATED. THUS, PROSPECTS APPEAR GOOD FOR ITALY TO CONTINUE TO MEET THESE TARGETS.

TABLE 5

COST-OF-LIVING ESCALATOR INDEX  
(AUGUST-OCTOBER 1974 EQUALS 100)

|             | 1977    | 1978    |         |         |
|-------------|---------|---------|---------|---------|
|             | JAN/APR | APR/JUL | JUL/OCT | OCT/JAN |
| IMF TARGET: |         |         |         |         |

|        |     |     |     |     |
|--------|-----|-----|-----|-----|
| INDEX  | 150 | 156 | 161 | 165 |
| POINTS | 7   | 6   | 5   | 4   |

ACTUAL:

|        |     |        |
|--------|-----|--------|
| INDEX  | 149 | 155 1) |
| POINTS | 6   | 5 1)   |

1) EMBASSY ESTIMATE.

7. CURRENT ACCOUNT OF BALANCE OF PAYMENTS. THE IMF TARGET FOR THE CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS APPLIES ONLY TO THE IMF STANDBY YEAR (APRIL 1, 1977 TO MARCH 31, 1978). HOWEVER, THE EMBASSY HAS OBTAINED FROM THE BANK OF ITALY SOME ROUGH QUARTERLY ESTIMATES OF THE DESEASONALIZED CURRENT ACCOUNT BALANCES WHICH WOULD ALLOW ITALY TO ACHIEVE ITS 500 BILLION LIRE SURPLUS FOR THE STANDBY YEAR. THESE BOI QUARTERLY FORECAST ASSUME A DEFICIT DURING CY 1977 OF 500 BILLION LIRE. THE EMBASSY HAS ROUGHLY DESEASONALIZED ACTUAL CURRENT ACCOUNT DATA FOR THE FIRST QUARTER. THE RESULT SUGGESTS THAT

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ITALY WAS WITHIN THE IMPLIED FIRST QUARTER TARGET. FURTHERMORE, BASED ON ITS LATEST FORECAST, THE EMBASSY BELIEVES THAT ITALY'S CURRENT ACCOUNT MAY ACTUALLY BE IN BALANCE DURING CY 1977, RATHER THAN BEING IN DEFICIT BY 500 BILLION LIRE. IF SO, THEN PROSPECTS FOR ACHIEVING A 500 BILLION LIRE SURPLUS DURING THE STANDBY YEAR ARE CORRESPONDINGLY IMPROVED.

## TABLE 6

CURRENT ACCOUNT OF BALANCE OF PAYMENTS  
(BILLIONS OF LIRE)

|                  |                     |
|------------------|---------------------|
| 1977             | 5-,\$?6 63-4        |
|                  | (4/1/77-            |
|                  | 3/31/78)            |
| I                | CY                  |
| IMF TARGET       |                     |
| (DESEASONALIZED) | -600 1) -500 1) 500 |
| ACTUAL           |                     |
| (DESEASONALIZED  | -558 2)             |
| (RAW)            | -814                |

1) BANK OF ITALY FORECAST OF PATTERN OF CURRENT ACCOUNT BALANCES ON DESEASONALIZED BASIS.  
2) ROUGH EMBASSY DESEASONALIZATION OF ACTUAL FIRST QUARTER DATA.

8. COMMENT. IN PREPARING THIS REPORT AND THE BACKGROUND AIRGRAM, THE EMBASSY HAS BECOME AWARE THAT MONITORING OF THE IMF/EC TARGETS IS MORE COMPLEX THAN MIGHT APPEAR ON THE SURFACE. THIS IS MAINLY DUE TO THE ABSENCE OF QUARTERLY TARGETS IN SOME CASES AND TO THE EXISTENCE OF MULTIPLE SOURCES OF STATISTICAL DATA WHICH ARE NOT CONCEPTUALLY COMPARABLE. THEREFORE, THE EMBASSY WOULD LIKE TO CAUTION WASHINGTON AGENCIES AS TO THE RELIABILITY OF THE EMBASSY'S ASSESSMENTS OF PERFORMANCE.

GARDNER

#1852

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## Message Attributes

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**Concepts:** REPORTS, DATA, LOANS, FINANCIAL AGREEMENTS  
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**Copy:** SINGLE  
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**Decaption Date:** 01-Jan-1960 12:00:00 am  
**Decaption Note:**  
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**Disposition Approved on Date:**  
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**Disposition Event:**  
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**Original Handling Restrictions:** n/a  
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**Status:** NATIVE  
**Subject:** ITALIAN PERFORMANCE UNDER IMF AND EC LOANS  
**TAGS:** EFIN, IT  
**To:** STATE TRSY  
**Type:** TE  
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